

Message Text

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ACTION EA-09

INFO OCT-01 ISO-00 AID-31 SS-15 SP-02 L-03 EB-07 CIAE-00

INR-07 NSAE-00 COME-00 FTC-01 TRSE-00 IO-13 NSC-05

H-02 STR-04 CIEP-01 /101 W
----- 094710

R 060725Z MAY 76
FM AMEMBASSY SEOUL
TO SECSTATE WASHDC 6975

C O N F I D E N T I A L SEOUL 3356

E.O. 11652: GDS
TAGS: EIND, KS
SUBJECT: AID NEGOTIATIONS

1. AS THE DEPARTMENT IS AWARE, AMERICAN INTERNATIONAL GROUP HAS BEEN NEGOTIATING WITH THE ROKG FOR SOME TIME IN AN ATTEMPT TO ENTER THE DOMESTIC INSURANCE MARKET HERE. THUS FAR, THESE NEGOTIATIONS HAVE FAILED TO PRODUCE AN AGREEMENT. THE MATTER HAS NOW BEEN ADDED TO THE AGENDA FOR THE SEVENTH MINISTERIAL CONFERENCE, WE UNDERSTAND AT THE SUGGESTION OF AIG; HENCE, THIS REPORT. WE HAD LONG PLANNED TO REPORT THE STATUS OF THESE NEGOTIATIONS, BUT DEFERRED DOING SO BECAUSE AGREEMENT ALWAYS SEEMED JUST AROUND THE CORNER.

2. AIG INITIALLY HAD DECIDED TO START A JOINT INSURANCE VENTURE WITH WASHIN, BUT THIS FIRM HAD NOT PREVIOUSLY BEEN IN THE INSURANCE BUSINESS, SO THE KOREAN GOVERNMENT REFUSED TO AUTHORIZE ITS ENTRANCE AT THIS TIME. AFTER CONSIDERABLE INTERNAL DEBATE, THE ROKG DECIDED TO AUTHORIZE THE THIRTEEN EXISTING KOREAN INSURANCE COMPANIES TO ENTER A JOINT VENTURE WITH AIG. NEGOTIATIONS HAVE BEEN GOING ON SPORADICALLY SINCE.

3. SEVERAL ISSUES REMAIN UNRESOLVED. INITIALLY, AID HAD WANTED TO ENTER THE KOREAN MARKET UNDER THE PROTECTION OF THE FOREIGN CAPITAL INDUCEMENT LAW. AIG BELIEVED IT HAD ORAL AGREEMENT ON THE POINT. WE ARE UNCERTAIN, BUT THE QUESTION

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OF PRIOR AGREEMENT HAS BEEN MADE MOOT BY THE DECISION OF THE ROKG

TO AMEND THE FOREIGN CAPITAL INDUCEMENT LAW. ONE OF THE BASIC PRINCIPLES OF THE REVISION IS TO DISCRIMINATE AMONG BUSINESS ACTIVITIES AND TO ACCORD THOSE LEAST DESIRED NO BENEFITS. INSURANCE HAS BEEN DETERMINED TO FALL IN THAT CATEGORY AND, IN ACCORD WITH ITS POLICY, THE GOVERNMENT WILL NOT AUTHORIZE AIG TO ENTER THE KOREAN MARKET UNDER THE EXISTING LAW.

4. AT THE SAME TIME, THE KOREAN GOVERNMENT HAS AGREED TO PROVIDE NORMAL GUARANTIES ON THE REPATRIATION OF PROFITS AND PRINCIPAL. IT HAS ALSO AGREED THAT AIG MAY OWN UP TO 45 PERCENT OF THE JOINT VENTURE AND HAVE OPERATING CONTROL THROUGH CORPORATE BYLAWS WHICH WOULD REQUIRE A TWO-THIRDS MAJORITY OF THE BOARD OF DIRECTORS. WE ASSUME THAT AIG WOULD GET A MANAGEMENT CONTRACT, AS WELL, IF NEGOTIATIONS GET TO THAT POINT.

5. THE MAJOR ISSUES STILL UNRESOLVED RELATE TO APPLICATION OF THE "GOING PUBLIC" ACT, WHICH PROVIDES SUBSTANTIAL TAX BENEFITS TO COMPANIES WHICH SELL AT LEAST 49 PERCENT OF THEIR SHARES TO THE PUBLIC. THE NEGOTIATOR FOR THE THIRTEEN KOREAN COMPANIES HAS SAID THAT THEY WOULD REQUIRE AIG TO REDUCE ITS EQUITY TO 30 PERCENT. AID HAS ARGUED THE INVESTMENT WOULD THEN BE UNATTRACTIVE TO THEM, SINCE THE JOINT VENTURE WOULD NOT HAVE AN EARNINGS TRACK RECORD TO MAKE PUBLIC SALE PROFITABLE, WHILE AIG WOULD THEREBY LOSE ONE THIRD OF ITS CLAIM ON FUTURE EARNINGS.

6. TWO OTHER ISSUES REMAIN UNRESOLVED. ONE IS THE BASIS ON WHICH THE JOINT VENTURE WILL PARTICIPATE IN THE INSURANCE POOL. THE OTHER IS THE TERMS ON WHICH AIG EXISTING BUSINESS IN KOREA SERVING THE EXPATRIATE COMMUNITY SHOULD BE TURNED OVER TO THE JOINT VENTURE. WE BELIEVE THERE IS A BASIS FOR COMPROMISE ON THESE ISSUES, BUT THAT NO DECISION WILL BE MADE UNTIL THE MAJOR ISSUE IS RESOLVED.

7. AIG'S ENTHUSIASM FOR THE JOINT VENTURE WITH THIRTEEN PARTNERS HAS NEVER BEEN GREAT. THEY BELIEVE THEY WOULD HAVE CONSIDERABLE DIFFICULTY IN ACHIEVING AGREEMENT AND DEVELOPING A CONSENSUS WHICH WOULD BE ESSENTIAL TO A SMOOTH OPERATION. THE THIRTEEN KOREAN JOINT VENTURE PARTNERS HAVE EXHIBITED A SIMILAR LACK OF ENTHUSIASM. GIVEN ITS INABILITY TO REACH WHAT IT CONSIDERED ACCEPTABLE TERMS, AIG HAS NOW BEGUN DISCUSSIONS WITH ONE OF THE

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THIRTEEN EXISTING KOREAN INSURANCE COMPANIES WITH A VIEW TO STARTING A JOINT VENTURE. THIS COMPANY, KORYO FIRE AND MARINE INSURANCE CO., LTC., A SUBSIDIARY OF SSANGYONG, HAS ALREADY GONE PUBLIC. AIG WOULD PREFER A SINGLE PARTNER IF IT MUST GO PUBLIC. HOWEVER, NEGOTIATIONS HAVE NOT GONE BEYOND AN EXPRESSION OF MUTUAL INTEREST, SO AIG DOES NOT KNOW WHAT THE TERMS OF A JOINT VENTURE MIGHT BE. IT IS PLANNING TO EXPLORE THOSE TERMS WITH KORYO OVER THE COMING WEEKS. WE ARE TOLD BY THE LOCAL AIG

REPRESENTATIVE THAT AIG WILL THEN HAVE A BASIS FOR COMPARING THE KORYO OPTION AND THE THIRTEEN PARTNER OPTION AS WELL AS THE OPTION OF NOT ENTERING THE DOMESTIC MARKET AT ALL.

8. WE HAVE SPENT CONSIDERABLE TIME ATTEMPTING TO KEEP THE DISCUSSIONS GOING AND TO CLARIFY POSITIONS AND THE MOTIVATIONS OF THE TWO PARTIES, INCLUDING AMBASSADOR'S DISCUSSIONS WITH DPM NAM. THIS HAS NOT ALWAYS BEEN EASY, SINCE THERE HAS BEEN SOME FEELING OF LACK OF GOOD FAITH ON EACH SIDE. THE FINANCE MINISTER RECENTLY INDICATED HE HAD CONSIDERABLE DIFFICULTY PERSUADING THE ROKG TO LET EVEN ONE FOREIGN FIRM IN. HE HAD SOLD THE THIRTEEN-PLUS-ONE JOINT VENTURE AS AN ATTRACTIVE PACKAGE TO AIG AND TO THE GOVERNMENT BECAUSE IT WOULD PRECLUDE OTHER FOREIGN FIRMS FROM ENTERING THE KOREAN MARKET. WE HAVE SUGGESTED TO THE GOVERNMENT THAT SOONER OR LATER THEY WOULD FIND IT IN THEIR INTEREST TO LET A NUMBER OF FOREIGN FIRMS IN, AND THAT THEY MIGHT BE BETTER ADVISED TO DO THIS SOONER RATHER THAN LATER. THE FINANCE MINISTER, HOWEVER, HAS INDICATED THAT GETTING THE GOVERNMENT TO CHANGE ITS POLICY NOW WOULD BE TIME CONSUMING AND DIFFICULT, IF NOT IMPOSSIBLE.

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Message Attributes

Automatic Decaptoning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: INSURANCE, NEGOTIATIONS, JOINT VENTURES, FOREIGN INVESTMENTS
Control Number: n/a
Copy: SINGLE
Draft Date: 06 MAY 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: izenbei0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976SEOUL03356
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Film Number: D760175-0031
From: SEOUL
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t19760583/aaaactlh.tel
Line Count: 136
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EA
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: izenbei0
Review Comment: n/a
Review Content Flags:
Review Date: 28 MAY 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <28 MAY 2004 by ShawDG>; APPROVED <22 SEP 2004 by izenbei0>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: AID NEGOTIATIONS
TAGS: EIND, EINV, KS, AMERICAN INTERNATIONAL GROUP
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006